

EXTERNAL AUDIT CIRCULAR No. 11



CONNECTICUT DEPARTMENT OF TRANSPORTATION

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SUBJECT: Employee Morale, Health and Welfare Costs

Effective Date: January 1, 2012

This Circular presents interpretative guidance regarding Employee Morale, Health and Welfare costs and includes examples for use in determining the allowability of such costs. Please refer to Chapter 8.8 of the 2010 edition of the AASHTO Uniform Audit & Accounting Guide for additional guidance

I. ISSUE

During indirect cost rate audits, auditors typically encounter costs such as the following:

- retirement gifts or performance awards, such as gold watches, gift certificates, and plaques;
- company picnics, outings, and holiday parties;
- flowers sent to employees or their families;
- registration fees for employer-sponsored sports teams;
- memberships to social organizations and country clubs; and
- memberships to fitness centers.

II. ALLOWABILITY

Employee welfare and morale expenses incurred on activities to improve working conditions, employer-employee relations, employee morale, and employee performance generally are allowable. Expenses for employee morale and welfare costs should be in compliance with FAR 31.205-13. The following paragraphs discuss certain of the costs listed above:

1. Reasonable costs for employee performance awards and retirement awards may be allowable charges to Federal contracts per FAR 31.205-13(b), when the awards are made pursuant to an established plan or policy or the awards are covered by FAR 31.205-6 compensation cost principle.
2. As stated in Chapter 8.8 of the AASHTO Audit Guide, the cost principles of FAR 31.205-13 (Employee Morale) and 31.205-14 (Entertainment), when read together, provide that costs for employee picnics, outings, and parties are unallowable.
3. Costs for flowers sent to employees or customers are unallowable per FAR 31.205-13(b), regardless of whether the company has an established policy in place that allows for the incurrence of such costs.
4. Costs for memberships to social organizations and country clubs are unallowable per the Entertainment Cost Principle at FAR 31.205-14. This is the case regardless of whether the cost is reported as taxable income to the employees.

III. EXAMPLES

Example 11-1. Upon retirement, each of Firm XYZ's employees receives a gold watch and \$500 gift certificate.

Analysis: Subject to reasonableness, these costs are allowable and may be included in indirect costs.

Example 11-2. Periodically, Firm XYZ purchases small gifts for employees, such as shirts, watches, or clocks embossed with the firm's logo.

Analysis: These costs are unallowable per FAR 31.205-13(b) and must be removed from indirect costs.

Example 11-3. Each year, Firm XYZ funds a holiday party for its employees.

Analysis: All costs associated with the party are unallowable entertainment (see FAR 31.205-14) and must be removed from indirect costs.

Example 11-4. As part of its benefits package, Firm XYZ will pay up to \$300 per year per employee for health club memberships.

Analysis: These costs are allowable per FAR 31.205-13 and may be included in indirect costs.

IV. REFERENCES

- FAR 31.205-13 (Employee Morale, Health, Welfare, Food Service, and Dormitory Costs and Credits).
- FAR 31.205-14 (Entertainment Costs).
- DCAA Contract Audit Manual § 7-2103.1 (interpretive guidance regarding the allowability of costs associated with company-sponsored picnics, outings, and parties).
- CTDOT External Audit Circular No. 1 (definitions, audit authority, and general guidance regarding the computation of overhead rates).
- CTDOT External Audit Circular No. 8 (Meals, Lodging, and Incidental Expenses)
- AASHTO Uniform Audit & Accounting Guide [2010 Edition]